

**Financial Statements**

**Barry County Community  
Mental Health Authority**

**Hastings, Michigan**

**September 30, 2004**



# Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name <b>Barry County Community Mental Health</b>	County <b>Barry</b>
Audit Date <b>9/30/04</b>	Opinion Date <b>12/21/04</b>	Date Accountant Report Submitted to State: <b>3/25/05</b>	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☒ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ Yes ☒ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ Yes ☐ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☒ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☒ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ Yes ☒ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☒ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☒ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☒ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

## We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	✓		
Reports on individual federal financial assistance programs (program audits).			✓
Single Audit Reports (ASLGU).			✓

Certified Public Accountant (Firm Name) <b>ROSLUND, PRESTAGE &amp; CO., PC, CPA'S</b>			
Street Address <b>308 GRATIOT AVENUE</b>		City <b>ALMA</b>	State <b>MI</b>
Accountant Signature <i>Ch. P. + CPA</i>		ZIP <b>48801</b>	Date <b>3/25/05</b>

Barry County Community Mental Health Authority  
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September 30, 2004

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## **INDEPENDENT AUDITOR'S REPORT**

Barry County Community Mental Health Authority  
Hastings, Michigan

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Barry County Community Mental Health Authority (the Authority), as of and for the year ended September 30, 2004, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Authority, as of September 30, 2004, and the respective changes in financial position and cash flows, where applicable, for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 21, 2004 on our consideration of the Authority's internal control over financial reporting and our test of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis on pages I-IV, and budgetary comparison information on page 25, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Authority's basic financial statements. The other supplemental financial information listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Roslund, Prestage & Co P.C.*  
Roslund, Prestage & Company, P.C.  
Certified Public Accountants

December 21, 2004

**MANAGEMENT'S DISCUSSION and ANALYSIS**

**Barry County Community Mental Health Authority**  
**Financial Statements for the Fiscal Year Ended September 30, 2004**  
**Management's Discussion and Analysis**

The management of Barry County Community Mental Health Authority (BCCMHA) presents the following overview and analysis of financial activities during the past fiscal year. BCCMHA was created as a Mental Health Authority effective March 1, 2002.

Overview of Financial Statements

Two types of financial statements are provided: Government-wide Statements and Fund Statements.

The government-wide financial statements are designed to provide readers with a broad overview of the organization's finances in a manner similar to a private sector business.

**The Statement of Net Assets** presents information on all of BCCMHA's assets and liabilities with the difference between assets and liabilities being reported as net assets. Changes in net assets serve as a useful indicator in determining whether the financial position is improving or deteriorating.

**The Statement of Activities** presents information showing how net assets changed during the fiscal year. Reporting of activities is on an accrual basis meaning that the change in net assets is reported as soon as the underlying event giving rise to the change occurs regardless of the timing of the related movement of cash.

The fund financial statements report groupings of related accounts that are used to maintain control over resources that have been segregated for specific activities or objectives. BCCMHA, as a governmental authority, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. These funds are divided into two categories: governmental funds and proprietary funds.

**Governmental funds/General Fund** has a narrower focus than that of the government-wide financial statements in that its focus is on the short-term movement of spendable resources and on the balances of spendable resources available at the end of the fiscal year.

**Proprietary fund** is an internal service fund which is held as a self-insurance against future risk. This fund consists of State of Michigan General Funds and accumulated interest and must be held for future risk or used to provide authorized services to eligible persons.

A crosswalk between government-wide and fund statements is included as Appendix A to this discussion. By comparing the two types of statements, the reader may better understand the long-term impact of the organization's immediate year decisions.

#### Comparison with Prior Year

Fiscal year 2003 revenues were \$4,045,447 compared to fiscal year 2004 revenues of \$4,653,404. This increase was mainly attributable to an increase in Medicaid funding and the introduction of the Adults Benefit Waiver which is explained below. Fiscal year 2003 expenses were \$4,170,931 compared to fiscal year 2004 expenses of \$4,546,072. This increase was attributed to several things including two new staff positions, annual salary increases, capital expenditures, and an increase in number of services provided.

#### Strength of Financial Position

Changes in financial position which help ensure the agency's future ability to provide services are:

	Balance at 10/1/2003	Increase (Decrease)	Balance at 9/30/04
Internal Service Funds			
Total Internal Service Funds	<u>\$142,949</u>	<u>1,199</u>	<u>\$144,148</u>
General Fund			
Fund Balance			
Restricted	57,833	3,931	61,764
Unrestricted	<u>199,381</u>	<u>136,262</u>	<u>335,643</u>
Total Fund Balance	\$257,214	\$140,193	\$397,407

The Internal Service Fund together with the unrestricted fund balance of the General Fund represents an estimated 38.5 days of operations based on daily operational needs.

#### About Fiscal Year 2004

In fiscal year 2004, BCCMHA invested in certificates of deposit in an effort to maximize interest. A laddering system was used to allow maximum investing without restricting large amounts of agency cash. Total interest earned during the year was \$2,079.39.

BCCMHA enrolled four consumers in the Habilitation Supports waiver program through Medicaid. This program allows for additional services for consumers residing in specialized residential homes who would otherwise reside in an institution. This provided \$28,967.61 in additional funding for fiscal year 2004.



The Adults Benefits Waiver was introduced as a new funding stream in 2004. This new category provided benefit to consumers who were originally covered under the Medicaid State Medical plan. This plan allows coverage of a list of selected services. BCCMHA received \$181,796.37 in funding. \$73,033 was spent on consumers in this category resulting in \$108,763.37 that may be carried forward and classified as local funding per the 2004/2005 general fund contract amendment.

In fiscal year 2004, two new positions were added to agency staff. A new computer server, copier and fax were purchased. Additions of this new equipment will achieve a higher level of efficiency and cost effectiveness. Due to lease expiration on an agency van used in Day Program services, a new van was purchased. After researching all options, a decision was made to purchase the vehicle in lieu of leasing.

Due to the uncertain nature of state budget, BCCMHA was again conservative in spending. Minimal but necessary purchases were made as described above. BCCMHA was fortunately not the target of any budget reductions.

#### About the Future

The State of Michigan is still projecting a budget shortfall both in fiscal year 2005 and 2006. Due to minimal effects of previous budget reductions, it is anticipated that mental health will experience some type of reduction in either or both years. With this in mind, the agency will continue to remain conservative, scrutinizing spending. With a challenging state economy, delivering quality services will remain the primary focus and challenge.

**Appendix A**  
**Crosswalk: Government-wide Statement of Assets and Funds Statements**

	Government Wide	General Fund	Governmental Activities/ISF	Fixed Assets	Long-term Debt
<b>Assets</b>					
Current Assets					
Cash and cash equivalents	\$903,754	\$759,606	\$144,148		
Accounts receivable	7,458	7,458			
Due from other governmental units	20,643	20,643			
Prepaid items	<u>61,764</u>	<u>61,764</u>			
Total current assets	<u>993,619</u>	<u>849,471</u>	<u>144,148</u>		
Noncurrent assets					
Capital assets - depreciable, net	<u>132,989</u>			<u>\$132,989</u>	
Total Assets	<u>1,126,608</u>	<u>849,471</u>	<u>144,148</u>	<u>132,989</u>	
<b>Liabilities</b>					
Current liabilities					
Accounts payable	168,867	168,867			
Accrued wages and other payroll liabilities	66,271	66,271			
Deferred revenue	83,856	83,856			
Due to other governmental units	<u>133,070</u>	<u>133,070</u>			
Total current liabilities	<u>452,064</u>	<u>452,064</u>			
Noncurrent liabilities					
Compensated absences	<u>131,924</u>				<u>\$131,924</u>
Total Liabilities	<u>583,988</u>	<u>452,064</u>			<u>131,924</u>
<b>Net Assets/Fund Balance</b>					
Invested in capital assets, net of related debt	132,989				
Reserved for risk management	144,148		144,148	132,989	
Unrestricted	<u>265,483</u>	<u>397,407</u>			
Total Net Assets/Fund Balance	<u>542,620</u>	<u>397,407</u>	<u>144,148</u>	<u>132,989</u>	

**BASIC FINANCIAL STATEMENTS -  
GOVERNMENT WIDE FINANCIAL STATEMENTS**

Barry County Community Mental Health Authority  
Statement of Net Assets  
September 30, 2004 and 2003

	Governmental Activities	
	2004	2003
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$903,754	\$1,099,193
Accounts receivable	7,458	\$7,048
Due from other governmental units	20,643	52,348
Prepaid items	61,764	57,833
Total current assets	993,619	1,216,422
Noncurrent assets		
Capital assets - depreciable, net	132,989	132,641
Total assets	1,126,608	1,349,063
<b>Liabilities</b>		
Current liabilities		
Accounts payable	168,867	176,741
Accrued wages and other payroll liabilities	66,271	49,528
Deferred revenue	83,856	-
Due to other governmental units	133,070	589,990
Total current liabilities	452,064	816,259
Noncurrent liabilities		
Note payable	-	31,500
Compensated absences	131,924	105,438
Total noncurrent liabilities	131,924	136,938
Total liabilities	583,988	953,197
<b>Net Assets</b>		
Invested in capital assets, net of related debt	132,989	101,141
Restricted for risk management	144,148	142,949
Unrestricted	265,483	151,776
Total net assets	\$542,620	\$395,866

See Accompanying Notes To Financial Statements

Barry County Community Mental Health Authority  
Statement of Activities  
For the Year Ended September 30, 2004 and 2003

Functions	Program Revenues			Net (Expense) Revenue and Changes Net Assets	2003
	Expenses	Charges for Services	Operating Grants and Contributions		
Governmental activities					
Health & Welfare - Mental Health	<u>\$4,540,710</u>	<u>\$2,753,030</u>	<u>\$1,894,549</u>	\$106,869	(\$342,317)
General revenues					
Unrestricted investment earnings				5,825	12,788
Restricted investment earnings				<u>1,199</u>	<u>3,230</u>
Total general revenues and contributions				<u>7,024</u>	<u>16,018</u>
Change in net assets				113,893	(326,299)
Net assets - beginning of year				395,866	738,214
Prior period adjustment				<u>32,861</u>	<u>(16,049)</u>
Net assets - end of year				<u>\$542,620</u>	<u>\$395,866</u>

See Accompanying Notes To Financial Statements

## **FUND FINANCIAL STATEMENTS**

Barry County Community Mental Health Authority  
Balance Sheet  
Governmental Funds  
September 30, 2004 and 2003

	General Fund	
	2004	2003
<b>Assets</b>		
Cash and cash equivalents	\$759,606	\$956,244
Accounts receivable	7,458	7,048
Due from other governmental units	20,643	52,348
Prepaid items	61,764	57,833
Total assets	<u>\$849,471</u>	<u>\$1,073,473</u>
<b>Liabilities</b>		
Accounts payable	\$168,867	\$176,741
Accrued wages and other payroll liabilities	66,271	49,528
Deferred revenue	83,856	-
Due to other governmental units	133,070	589,990
Total liabilities	<u>452,064</u>	<u>816,259</u>
<b>Fund balances</b>		
Reserved for prepaid items	61,764	57,833
Unreserved	335,643	199,381
Total fund balances	<u>397,407</u>	<u>257,214</u>
Total liabilities and fund balances	<u>\$849,471</u>	<u>\$1,073,473</u>

See Accompanying Notes To Financial Statements

Barry County Community Mental Health Authority  
Reconciliation of Fund Balances on the Balance Sheet for Governmental Funds  
to Net Assets of Governmental Activities on the Statement of Net Assets  
For the Year Ended September 30, 2004

Total fund balance - governmental funds	\$397,407
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	
Add: capital assets	314,544
Deduct: accumulated depreciation	(181,555)
An internal service fund is used by management to cover the risk of overspending the Managed Care Specialty Services Program contract. The assets and liabilities of the internal service fund are included in governmental activities in the statement of net assets.	
Add: net assets of governmental activities accounted for in the internal service fund	144,148
Some liabilities are not due and payable in the current period and, therefore, are not reported in the funds. Those liabilities consist of:	
Deduct: Compensated absences	<u>(131,924)</u>
Net assets of governmental activities	<u><u>\$542,620</u></u>

See Accompanying Notes To Financial Statements



Barry County Community Mental Health Authority  
Statement of Revenues, Expenditures and Changes in Fund Balances  
Governmental Funds  
For the Year Ended September 30, 2004 and 2003

<b>REVENUES</b>	<u>2004</u>	<u>2003</u>
State grants		
Department of Community Health Contract		
General Fund Formula and Categorical	\$1,497,848	\$1,859,102
Adult Benefit Waiver	181,796	-
Other state grants	40,565	35,579
Total state grants	<u>1,720,209</u>	<u>1,894,681</u>
Federal grants	<u>13,160</u>	<u>14,175</u>
Contributions - local units		
County appropriations	<u>154,500</u>	<u>145,000</u>
Charges for services		
Medicaid	2,663,552	1,881,368
Client and third party pay	89,478	78,177
Total charges for services	<u>2,753,030</u>	<u>1,959,545</u>
Interest and rents		
Interest	<u>5,825</u>	<u>12,788</u>
Other revenue		
Miscellaneous	<u>6,680</u>	<u>19,258</u>
Total revenues	4,653,404	4,045,447
<b>EXPENDITURES</b>		
Health & Welfare - Mental Health		
Personnel costs	2,131,531	1,925,604
Operating expenditures	2,345,673	2,210,407
Capital outlay	37,368	3,420
Debt service	<u>31,500</u>	<u>31,500</u>
Total expenditures	<u>4,546,072</u>	<u>4,170,931</u>
Revenues over (under) expenditures	107,332	(125,484)
Other financing sources (uses)		
Operating transfers out - other governmental units	<u>-</u>	<u>(101,423)</u>
Excess of revenues and other sources over expenditures and other uses	107,332	(226,907)
Fund balance, beginning of year	257,214	500,170
Prior period adjustment	<u>32,861</u>	<u>(16,049)</u>
Fund balance, end of year	<u>\$397,407</u>	<u>\$257,214</u>

See Accompanying Notes To Financial Statements

Barry County Community Mental Health Authority  
Reconciliation of the Statement of Revenues, Expenditures  
and Changes in Fund Balances of Governmental Funds  
to the Statement of Activities  
For the Year Ended September 30, 2004

Net change in fund balances - total governmental funds	\$107,332
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense.	
Add: capital outlay	37,368
Deduct: depreciation expense	(36,320)
An internal service fund is used by management to cover the risk of overspending the Managed Care Specialty Services Program contract. The net revenue (expense) of the fund attributable to those funds is reported with governmental activities.	
Add: interest income from governmental internal service fund	1,199
Payment of principal on long-term debt is an expenditure in the governmental funds, but not in the statement of activities (where it reduces long-term debt).	31,500
Sale of capital asset proceeds are recognized as revenues in the governmental funds, but only the gain / loss is recognized in the statement of activities	(700)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the funds.	
Less: Increase in accrual for compensated absences	(26,486)
Change in net assets of governmental activities	<u>\$113,893</u>

See Accompanying Notes To Financial Statements

Barry County Community Mental Health Authority  
Statement of Net Assets  
Proprietary Funds  
September 30, 2004 and 2003

	<u>Internal Service Funds</u>	
	<u>2004</u>	<u>2003</u>
Assets		
Cash and cash equivalents	<u>\$144,148</u>	<u>\$142,949</u>
Net assets		
Restricted	<u>\$144,148</u>	<u>\$142,949</u>

See Accompanying Notes To Financial Statements

Barry County Community Mental Health Authority  
Statement of Revenues, Expenses and Changes in Fund Net Assets  
Proprietary Funds  
For the Year Ended September 30, 2004 and 2003

	<u>Internal Service Funds</u>	
	<u>2004</u>	<u>2003</u>
Non-operating revenues		
Interest income	\$1,199	\$3,230
Operating transfers		
Operating transfers out - other governmental units	<u>-</u>	<u>(99,287)</u>
Change in net assets	1,199	(96,057)
Net assets, beginning of year	<u>142,949</u>	<u>239,006</u>
Net assets, end of year	<u><u>\$144,148</u></u>	<u><u>\$142,949</u></u>

See Accompanying Notes To Financial Statements

Barry County Community Mental Health Authority  
Statement of Cash Flows  
Proprietary Funds  
For the Year Ended September 30, 2004 and 2003

	<u>Internal Service Funds</u>	
	<u>2004</u>	<u>2003</u>
Cash flows from operating activities	-	-
Cash flows from noncapital financial activities		
Operating transfers out	-	(\$99,287)
Cash flows from investing activities		
Proceeds from interest earnings	<u>\$1,199</u>	<u>3,230</u>
Net increase (decrease) in cash	1,199	(96,057)
Cash and cash equivalents, beginning of year	<u>142,949</u>	<u>239,006</u>
Cash and cash equivalents, end of year	<u><u>\$144,148</u></u>	<u><u>\$142,949</u></u>
Reconciliation of operating income to net cash provided by (used for) operating activities:		
Operating income (loss)	-	-

See Accompanying Notes To Financial Statements

**NOTES TO THE FINANCIAL STATEMENTS**

Barry County Community Mental Health Authority  
Notes to the Financial Statements

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies of the Barry County Community Mental Health Authority (the Authority) conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the significant accounting policies used by the Authority.

In June of 1999, the GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. The significant changes included in Statement No. 34 include the following:

- A Management's Discussion and Analysis (MD&A) section providing an analysis of the Authority's overall financial position and results of operations.
- Financial statements prepared using full accrual accounting for all of the Authority's activities.
- A change in the fund financial statements to focus on major funds.

These and other changes are reflected in the accompanying financial statements (including the notes to the financial statements). The Authority has implemented the provisions of Statement No. 34 effective October 1, 2002.

**Reporting Entity**

The Authority operates as a Community Mental Health Authority under the provisions of Act 258 - Public Acts of 1974, as amended. The Authority provides funding for services in the areas of mental illness, developmental disabilities, and other related mental health needs for residents of Barry County.

The accompanying financial statements have been prepared in accordance with criteria established by the Governmental Accounting Standards Board for determining the various governmental organizations to be included in the reporting entity. These criteria include significant operational financial relationships that determine which of the governmental organizations are a part of the Authority's reporting entity, and which organizations are legally separate, component units of the Authority. Based on the application of the criteria, the Authority does not contain any component units.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

**Government-Wide and Fund Financial Statements**

The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the Authority. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges to consumers who purchase, use or directly benefit from services provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues.

Net assets are restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally it is the Authority's policy to use restricted resources first, then unrestricted resources as they are needed.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

**Measurement Focus, Basis of Accounting and Financial Statement Presentation**

Government-Wide Financial Statements – The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.



Barry County Community Mental Health Authority  
Notes to the Financial Statements

Governmental Fund Financial Statements - The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Authority considers revenues to be available if they are collected within 60 days of the end of the current fiscal year end.

An exception to the "60 day" rule is the recognition of certain patient fee revenues and the related receivables. The Authority has elected to recognize these revenues on the cash basis of accounting, which is in compliance with the Department of Community Health's revenue recognition formula. The difference between the cash basis of accounting and modified accrual basis of accounting for these revenues are not material to the financial statements.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

Modifications to the accrual basis of accounting include:

- Employees' vested annual leave is recorded as expenditures when utilized. The amount of accumulated annual leave unpaid at September 30, has been reported only in the government-wide financial statements.
- Interest on general long-term obligations is recognized when paid.
- Debt service expenditures and claims and judgments are recorded only when payment is due.

Proprietary Fund Financial Statements - The financial statements of the proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. The principal operating revenues of the internal service fund are charges to other funds for insurance services. Operating expenses for internal service funds include the cost of claims, administration and reinsurance. Any revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

The Authority reports the following major governmental and proprietary funds:

Governmental Funds

General Fund – This fund is the Authority's primary operating fund. It accounts for all financial resources of the Authority, except those required to be accounted for in other funds.

Proprietary Funds

Internal Service Fund - This fund represents amounts set aside to fund the net uninsured exposure of potential shortfalls of contract revenues.

**Comparative Data**

Comparative total data for the prior year has been presented in order to provide an understanding of the changes in financial position and operations. Also, certain amounts presented in the prior year may have been reclassified in order to be consistent with the current year's presentation.

**Budgetary Data**

Budgets are adopted by the Authority for all governmental funds. The budget is adopted and prepared on the modified accrual basis of accounting. The budget is also adopted at the function level. The budgeted revenues and expenditures for governmental fund types, as presented in this report, include any authorized amendments to the original budget as adopted.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

**Cash and Cash Equivalents**

The Authority's cash and cash equivalents are considered to be cash on hand, money market funds, demand deposits and short-term investments with an original maturity of three months or less from the date of acquisition.

Michigan Compiled Laws, Section 129.91, authorizes the Authority to deposit and invest in the accounts of Federally insured banks, credit unions, and savings and loan associations; bonds, securities and other direct obligations of the United States, or any agency or instrumentality of the United States; United States government or Federal agency obligation repurchase agreements; bankers' acceptance of United States banks; commercial paper rated by two standard rating agencies within the two highest classifications, which mature not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions which are rated investment grade; and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan. Financial institutions eligible for deposit of public funds must maintain an office in Michigan. The Authority's deposits are in accordance with statutory authority.

**Receivables**

Accounts receivable in all funds report amounts that have arisen in the ordinary course of business and are stated net of allowances for uncollectible amounts.

Due from other governmental entities consist primarily of amounts due from the Michigan Department of Community Health and the State of Michigan.

**Prepaid Items**

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

**Inventories**

The Authority does not recognize as an asset inventories of supplies. The cost of these supplies is considered immaterial to the financial statements and the quantities are not prone to wide fluctuation from year to year. The costs of such supplies are expensed when purchased.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

**Fixed Assets**

Capital assets, which include property, plant and equipment, are reported in the governmental activities column in the government-wide financial statements. Capital assets are defined by the government as individual assets with an initial cost equal to or more than \$1,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

The Authority does not have infrastructure type assets.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during construction of capital assets is not capitalized. No interest expense was incurred during the current year.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements and proprietary fund financial statements.

Capital assets of the Authority are depreciated using the straight line method over the following estimated useful lives:

Assets	Years
Computer Equipment	5
Furniture / Fixtures	5 - 15
Office Equipment	5 - 10
Automobiles	5

**Governmental Fund – Fund Balance Reserves and Designations**

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditure or (2) legally segregated for a specific future use. The reserves for related assets such as prepaid items are examples of the former.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

**Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

**Inpatient / Residential Cost Liability**

The amount recorded for inpatient/residential liability is based on management's estimate. This estimate is based on 1) the number of clients at each facility, 2) the number of days each client is at each facility, and 3) the daily rate charged for each facility.

The Authority does not receive actual billings for these services until several months after the service date. Therefore, the liability is not liquidated within the normal 60 day period after year end. Also, the actual cost may vary from the estimated due to reimbursements from third party payors that are applied to the total cost before the billings are sent to the Authority. This liability is included in accounts payable and due to other governmental units.

**NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

**Budgetary Information**

Annual budgets are adopted at the function level and on a basis consistent with generally accepted accounting principles for the general fund. All annual appropriations lapse at fiscal year end. The Authority does not maintain a formalized encumbrance accounting system. The budgeted revenues and expenditures, as presented in this report, include any authorized amendments to the original budget as adopted.

**Excess of Expenditures over Appropriations**

P.A. 621 of 1978, Section 18(1), as amended, provides that a local unit shall not incur expenditures in excess of the amount appropriated.

During the year ended September 30, 2004, the Authority incurred expenditures in excess of the amounts appropriated as shown on pages 25 of this report.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

**NOTE 3 – DETAIL NOTES**

**Cash and Investments**

At year-end, the carrying amount of the Authority's cash deposits was \$903,579, and the bank balance was \$1,054,936. Of the bank balance, \$100,000 was covered by federal depository insurance and the remaining, was uninsured and uncollateralized.

The Authority believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the Authority evaluates each financial institution with which it deposits government funds and accesses the level of risk of each institution. Only those institutions with an acceptable estimated risk level are used as depositories.

A reconciliation of cash and investments as shown on the Statement of Net Assets follows:

Cash deposits	\$903,579
Petty cash	175
Total	\$903,754

**Due from Other Governmental Units**

Due from other governmental units as of September 30, consists of the following:

	2004	2003
MDCH - OBRA Grant	\$1,302	\$2,592
MDCH – Juvenile Justice Grant	4,517	-
MDCH – Other Grants	1,331	13,402
Barry County	1,459	36,250
Calhoun County CMH Authority	12,034	104
Total	\$20,643	\$52,348

Barry County Community Mental Health Authority  
Notes to the Financial Statements

**Capital Assets**

Depreciable capital assets activity for the year ended September 30, 2004 was as follows:

<b>Governmental Activities</b>	<b>Beginning Balance</b>	<b>Additions</b>	<b>Disposals</b>	<b>Ending Balance</b>
Computer and Office Equipment	\$231,295	\$18,507	\$(10,820)	\$238,982
Furniture and Fixtures	51,352	-	-	51,352
Vehicles	5,349	18,861	-	24,210
Sub-totals	287,996	37,368	(10,820)	314,544
Accumulated Depreciation	(155,355)	(36,320)	10,120	(181,555)
Totals	\$132,641	\$1,048	\$(700)	\$132,989

Depreciation expense was charged to the Health & Welfare – Mental Health Program.

**Accrued Wages and Other Payroll Liabilities**

This liability represents amounts paid to employees during October that was earned during September. Also included are employer payroll taxes.

**Due To Other Governmental Units**

As of September 30, this liability consists of the following:

	<b>2004</b>	<b>2003</b>
State of Michigan - Inpatient Services	-	\$5,064
Department of Community Health – Cost Settlement	\$102,458	32,430
Department of Community Health – Risk Authorization Reduction	-	6,567
Calhoun County CMH Authority	\$30,612	545,929
Total	\$133,070	\$589,990

Barry County Community Mental Health Authority  
Notes to the Financial Statements

**Long Term Liabilities**

Compensated Absences

Authority policy allows full time employees to accumulate vacation times at various rates, depending on the employee's length of service with the Authority. As of September 30, 2004 and 2003, these liabilities totaled \$131,924 and \$105,438 respectively.

Note Payable

During the 2002 year, the Authority entered into a financing agreement for the purchase of computer software. The cost of this software was \$94,500. Payments are due annually in the amount of \$31,500. Interest rate is 0%. This note was paid in full during the 2004 fiscal year.

The changes in long term liabilities during the 2004 fiscal year are as follows:

Liability	Balance October 1, 2003	Additions	Reductions	Balance September 30, 2004
Compensated Absences	\$105,438	\$26,486	-	\$131,924
Note Payable	31,500	-	\$31,500	-
Totals	\$136,938	\$26,486	\$31,500	\$131,924



Barry County Community Mental Health Authority  
Notes to the Financial Statements

**Operating Leases**

The Authority has entered into various operating leases for the use of real property. Operating leases do not give rise to property rights or lease obligations, and therefore are not reported as assets or liabilities in these financial statements.

The following is a schedule of future minimum rental payments required under the operating leases that have initial or remaining noncancelable lease terms as of September 30th:

YEAR ENDING SEPTEMBER 30,	AMOUNT
2005	\$299,236
2006	299,236
2007	299,236
2008	75,133
2009	54,760
2010 - 2014	31,943

**NOTE 4 - OTHER INFORMATION**

**Risk Management**

Michigan Municipal Risk Management Authority

The Authority participated in the public entity risk pool – Michigan Municipal Risk Management Authority (MMRMA) for general liability coverage.

MMRMA, a separate legal entity, is a self-insured association organized under the laws of the State of Michigan to provide self-insurance protection against loss and risk management services to various Michigan governmental entities.

As a member of this pool, the Authority is responsible for paying all costs, including damages, indemnification, and allocated loss adjustment for each occurrence that falls within the member's self-insured retention (SIR). The Authority's SIR is between \$-0- and \$250. After the Authority's SIR and deductibles have been satisfied, MMRMA will be responsible for paying all remaining costs, including damages, indemnification, and allocated loss adjustment expenses to the limits of coverage stated below.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

Michigan Municipal Risk Management Authority (Continued)

MMRMA's coverage limits are between \$2,000 and \$5,000,000 for liability, and between \$10,000 and \$200,000,000 for property and crime.

The contribution made by the Authority to the MMRMA was \$19,059 for the period July 1, 2003 to July 1, 2004.

Risk Management – Internal Service Fund

During the September 30, 1998 fiscal year, the Authority authorized the establishment of an Internal Service Fund. This fund is used to cover the risk of overspending the Managed Care Specialty Services Program (MCSSP) contract. This contract provides for the use of Department of Community Health funding for the establishment of an Internal Service Fund, which is restricted to meet the expected future risk corridor requirements of the contract. Expenditures from the Internal Service Fund will occur when, in any one fiscal year, the Authority finds it necessary to expend more to provide services necessary to carry out the MCSSP contract requirements than revenue provided to the Authority by the contract.

**Employee Retirement and Benefit Systems**

**Plan Description**

The Authority participates in the Michigan Municipal Employees Retirement System (MERS), an agent multiple-employer defined benefit pension plan that covers all of the Authority's regular full-time employees. The system provides retirement, disability and death benefits to plan members and their beneficiaries. MERS issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to Gabriel, Roeder, Smith & Company, One Towne Square, Suite 800, Southfield, Michigan 48076.

The most recent period for which actuarial data was available was for the year ended December 31, 2003. The Authority's payroll for the employees covered by the system for the year ended December 31, 2003 was \$1,364,764.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

As of December 31, 2003, employee membership data related to the pension plan was as follows:

Retirees and beneficiaries currently receiving benefits	0
Active plan participants	43
Vested former members	3
Total	46

**Funding Policy**

Under the provisions of this plan, members contribute approximately ½ of 1% of annual compensation. If a member leaves the Authority or dies, without a retirement allowance or other benefit payable on his / her account, his / her accumulated contributions will be refunded to him / her, if living, or to his / her nominated beneficiary.

Benefit programs and provisions are established by the Retirement Board. All benefits vest after 10 years of service, except that benefits may vest after eight or six years of service if adopted by the municipality's governing body. The standard retirement age is 60 years; however, members may retire with several combinations of age and years of service and receive reduced early retirement benefits. Municipalities may adopt various other benefit programs which allow retirement at an earlier age with unreduced benefits based upon combinations of age and years of service, or just years of service. MERS also provides non-duty disability and death benefits to members after vesting requirements are met.

**Funding Status and Progress**

The amount shown below as the "pension benefit obligation" is based on the standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and separate benefits, estimated to be payable in the future as a result of employee services to date. The measure is the actuarial present value of credited projected benefits and is intended to (1) help users assess the plan's funding status of the system on a going-concern basis; (2) assess progress made in accumulating sufficient assets to pay benefits when due; and (3) make comparisons among public employee retirement plans. The measure is independent of the actuarial funding method used to determine contributions to the plan.

Barry County Community Mental Health Authority  
Notes to the Financial Statements

The pension benefit obligation was determined as part of an actuarial valuation of the plan as of December 31, 2003. Significant actuarial assumptions used in determining the pension benefit obligation include (a) a rate of return on the investment of present and future assets of 8.0% and (b) projected salary increases of 4.5% per year plus a percentage based on an age-related scale to reflect merit, longevity and promotional salary increases.

At December 31, 2003, the assets were less than the pension benefit obligation by \$556,112, determined as follows:

<b>GASB 25 Information</b>	
<b>Actuarial Accrued Liability</b>	
Retirees and beneficiaries currently receiving benefits	\$0
Terminated employees not yet receiving benefits	20,229
Non-vested terminated employees	3,285
Current Employees:	
Accumulated employee contributions including allocated investment income	91,321
Employer financed	1,667,276
Total actuarial accrued liability	1,782,111
Net assets available for benefits at actuarial value (market = \$1,119,469)	1,225,999
Unfunded actuarial accrued liability	\$556,112
<b>GASB 27 Information</b>	
Fiscal Year Beginning	April 1, 2005
Annual Required Contribution (ARC)	\$117,708
Amortization factor used – under-funded liabilities (30 years)	.053632

Barry County Community Mental Health Authority  
Notes to the Financial Statements

Three year trend information follows:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability	Unfunded AAL (UAAL)	Fund Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
12-31-01	(a)	(a)	(a)	(a)	(a)	(a)
12-31-02	994,410	1,452,890	(458,480)	69%	1,193,393	39%
12-31-03	1,225,999	1,782,111	(556,112)	69%	1,364,764	41%

(a) Effective March 1, 2002, the Authority was an independent MERS participating municipality. Prior to this date, the Authority was included in Barry County's pension plan.

### Compliance Audits

All governmental grants are subject to a transactional and compliance audit by the grantors or their representatives. Therefore, an indeterminable contingency exists for expenditures, which may be disallowed by the granting agencies.

### Prior Period Adjustment

The following transactions were recognized in these financial statements as prior period adjustments:

Description	2004	2003
Adjustment to prior year cost settlement document filed with the Michigan Department of Community Health	\$32,430	\$(6,567)
Adjustment to inpatient liability accrual	-	18,436
Write off of Medicaid receivables	-	(28,295)
Other	431	377
Total	\$32,861	\$(16,049)

**REQUIRED SUPPLEMENTAL INFORMATION**

Barry County Community Mental Health Authority  
Statement of Revenues, Expenditures and Changes  
in Fund Balance - Budget and Actual  
General Fund  
For the Year Ended September 30, 2004

	Budgeted Amounts			Variance Between Actual and Final Budget
	Original	Final	Actual	
REVENUES				
State grants				
Department of Community Health Contract				
General Fund Formula and Categorical	\$1,856,978	\$1,697,273	\$1,497,848	(\$199,425)
Adult Benefit Waiver	-	183,355	181,796	(1,559)
Other state grants	13,387	41,098	40,565	(533)
Total state grants	<u>1,870,365</u>	<u>1,921,726</u>	<u>1,720,209</u>	<u>(201,517)</u>
Federal grants	<u>16,500</u>	<u>16,500</u>	<u>13,160</u>	<u>(3,340)</u>
Contributions - local units				
County appropriations	<u>152,125</u>	<u>154,500</u>	<u>154,500</u>	<u>-</u>
Charges for services				
Medicaid	2,420,656	2,705,477	2,663,552	(41,925)
Client and third party pay	62,500	62,500	89,478	26,978
Total charges for services	<u>2,483,156</u>	<u>2,767,977</u>	<u>2,753,030</u>	<u>(14,947)</u>
Interest and rents				
Interest	<u>14,000</u>	<u>6,000</u>	<u>5,825</u>	<u>(175)</u>
Other revenue				
Miscellaneous	<u>3,700</u>	<u>3,700</u>	<u>6,680</u>	<u>2,980</u>
Total revenues	<u>4,539,846</u>	<u>4,870,403</u>	<u>4,653,404</u>	<u>(216,999)</u>
EXPENDITURES				
Health & Welfare - Mental Health				
Current:				
Personnel costs	2,133,691	2,185,848	2,131,531	54,317
Operating expenditures	2,370,425	2,419,487	2,345,673	73,814
Capital outlay	-	-	37,368	(37,368)
Debt service	<u>-</u>	<u>-</u>	<u>31,500</u>	<u>(31,500)</u>
Total expenditures	<u>4,504,116</u>	<u>4,605,335</u>	<u>4,546,072</u>	<u>59,263</u>
Revenues over (under) expenditures	35,730	265,068	107,332	(157,736)
Fund balance, beginning of year	257,214	257,214	257,214	-
Prior period adjustment	<u>-</u>	<u>-</u>	<u>32,861</u>	<u>32,861</u>
Fund balance, end of year	<u>\$292,944</u>	<u>\$522,282</u>	<u>\$397,407</u>	<u>(\$124,875)</u>

See Accompanying Notes To Financial Statements

**OTHER SUPPLEMENTARY INFORMATION**



Barry County Community Mental Health Authority  
Supporting Schedule of Personnel Costs  
For the Year Ending September 30, 2004 and 2003

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Governmental Fund Types

General Fund

	<u>2004</u>	<u>2003</u>
<b>Personnel costs</b>		
Salaries and wages	\$1,537,442	\$1,334,898
Fringe benefits	<u>594,089</u>	<u>590,706</u>
Total personnel costs	<u><u>\$2,131,531</u></u>	<u><u>\$1,925,604</u></u>

See Accompanying Notes To Financial Statements

Barry County Community Mental Health Authority  
Supporting Schedule of Operating Expenditures  
For the Year Ending September 30, 2004 and 2003

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Governmental Fund Types

General Fund

	<u>2004</u>	<u>2003</u>
<b>Operating expenditures</b>		
Communications	\$14,812	\$19,652
Contractual services	1,446,194	1,431,424
Inpatient services	316,394	193,437
Insurance	24,512	23,191
Medicaid local draw down	45,634	45,634
Meetings and conferences	8,036	11,120
Other	11,556	7,541
Rents	297,025	294,609
Repairs and maintenance	13,907	17,188
Printing and publishing	3,168	3,264
Supplies	35,560	38,268
Travel and transportation	121,869	118,577
Utilities	7,006	6,502
	<u>7,006</u>	<u>6,502</u>
 Total operating expenditures	 <u>\$2,345,673</u>	 <u>\$2,210,407</u>

See Accompanying Notes To Financial Statements



**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL  
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH  
GOVERNMENT AUDITING STANDARDS**

Barry County Community Mental Health Authority  
Hastings, Michigan

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Barry County Community Mental Health Authority (the Authority) as of and for the year ended September 30, 2004, which collectively comprise the Authority's basic financial statements and have issued our report thereon dated December 21, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

**Compliance**

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of the Authority, in a separate letter dated December 21, 2004.

This report is intended for the information of the audit committee, management, and the Board of Directors, and is not intended to be and should not be used by anyone other than these specified parties.

*Roslund, Prestage & Co, P.C.*

Roslund, Prestage & Company, P.C.  
Certified Public Accountants

December 21, 2004



## MANAGEMENT LETTER

Board of Directors  
Barry County Community Mental Health Authority  
Hastings, Michigan

In planning and performing our audit of the financial statements for Barry County Community Mental Health Authority for the fiscal year ended September 30, 2004, we considered the internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

However, during our audit we became aware of matters that are opportunities for strengthening internal controls. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters.

This letter does not affect our audit report dated December 21, 2004 on the financial statements of Barry County Community Mental Health Authority.

We will review the status of these comments during our next audit engagement. We have discussed these comments and suggestions with management, and will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Sincerely,

Roslund, Prestage & Company, P.C.  
Certified Public Accountants

December 21, 2004

### **Perform a Fraud Risk Assessment**

In light of the wave of notorious frauds involving large companies in the last few years, such as Enron, WorldCom, and HealthSouth, there may be a misperception that fraud affects only large companies. However, fraud occurs in companies of all sizes, and almost any employee may be capable of perpetrating a fraudulent act given the right set of circumstances. In fact, fraud may be a more significant problem for small companies. In the 2002 survey of its members conducted by the Association of Certified Fraud Examiners (ACFE), the median loss per fraud occurrence reported from businesses with 100 or fewer employees was \$127,500, a proportionately larger loss than the \$97,000 median loss in companies with 10,000 or more employees.

Whereas the highly publicized frauds at large public companies like Enron, WorldCom, and HealthSouth involved fraudulent financial reporting, for small companies, one of the primary fraud risks is the ever-present risk of misappropriation of assets (theft), particularly fraudulent cash disbursements. The opportunity to commit and conceal fraud exists where there are assets susceptible to misappropriation and there are inadequate controls to prevent or detect the fraud. To address this risk, we recommend that the Authority perform a risk assessment to identify, analyze, and manage the risk of asset misappropriation. Risk assessment, including fraud risk assessment, is one element of internal control. Thus, ideally, the Authority's internal control should include performance of this assessment, even though our annual financial statement audits include consideration of fraud.

During our audit, we have reviewed and tested the Authority's internal control system, and found no indication that fraud has occurred. However, a fraud risk assessment should be performed on a regular basis to timely identify any changes needed in the Authority's internal control system.

This assessment can be informal and performed by a management-level individual. Ordinarily, the management-level individual would conduct interviews or lead group discussions with personnel who have extensive knowledge of the Authority, its environment, and its processes. The fraud risk assessment process should consider the Authority's vulnerability to misappropriation of assets. When conducting the self-assessment, questions such as the following can be considered:

- Which individuals in the Authority have the opportunity to misappropriate assets? These are individuals who have access to assets susceptible to theft and to records that can be falsified or manipulated to conceal the theft.
- Are there any known pressures that would motivate individuals with the opportunity to misappropriate assets? Pressures may relate to financial stress or dissatisfaction. In assessing whether these pressures may exist, the assessor should consider whether there is any information that indicates potential financial stress or dissatisfaction of individuals with access to assets susceptible to misappropriation.

**Perform a Fraud Risk Assessment (continued)**

- What assets of the Authority are susceptible to misappropriation?
- Are there any known internal control weaknesses that would allow misappropriation of assets to occur and remain undetected?
- How could assets be stolen? Assets can be stolen in many ways besides merely removing them from the premises. For example, cash can be stolen by writing checks to fictitious individuals or vendors and cashing them for personal use. Inventory or other assets can be stolen through sales to fictitious customers.
- How could potential misappropriation of assets be concealed? Because many frauds create accounting anomalies, the perpetrator must hide the fraud by running it through as an adjustment to another account. Generally, fraud perpetrators may use accounts that are not closely monitored.
- What factors might indicate that the Authority has a culture or environment that would enable management or individuals to rationalize committing fraud?

Once areas vulnerable to fraud have been identified, a review of the Authority's systems, procedures, and existing controls relating to the identified areas should be conducted. The Authority should consider what additional controls need to be implemented to reduce the risk of fraud. There are two basic types of controls—those that are designed to address specific types of fraud, and those that are more general in nature. General controls that reduce an individual's ability to commit fraud without detection include the following:

- Requiring Periodic Job Rotation and Mandatory Vacations. When an employee stays in the same position for a long period and has few absences, an opportunity exists for that employee to design and commit fraud schemes. Requiring key individuals to rotate jobs periodically or to transfer to different job functions is one way to address this fraud risk. Requiring all individuals to take an annual vacation, during which time others perform their job functions, also makes it more difficult for an employee who is committing fraud to continue concealing the fraud scheme.
- Preparing and Reviewing Monthly Financial Statements in a Timely Fashion. As previously mentioned, many frauds create accounting anomalies. Thus, one way to detect fraud on a timely basis is to review monthly financial statements and investigate unusual variances. If possible, these statements should include budget, prior period, and year-to-date amounts to help identify variances. Performing the review and investigation on a timely basis helps minimize the extent of potential fraud.

### **Perform a Fraud Risk Assessment (continued)**

Examples of controls to prevent or detect specific types of fraud include the following:

- Independent Checks of work performed. Independent checks test another employee's work, such as by having a second employee re-perform or test an employee's work.
- Separation of Duties. Separation of duties is one of the most effective controls to prevent or detect misappropriations of assets. When possible, incompatible duties should be performed by different employees. For example, the responsibility for authorizing transactions, recording transactions, and maintaining custody of assets should be assigned to different people in the Authority to the extent possible.

When assessing the Authority's internal control, the relationship between the nature and extent of fraud controls recommended and the cost of implementing those controls should be considered. For example, instead of trying to prevent fraud, the Authority may choose to use more detective controls to ensure that the fraud is identified and corrected in a timely fashion. Because detective controls are performed after the original transaction occurs, they may be easier to implement and more cost effective.

We would be pleased to provide more information about performing a risk assessment or assist management in performing one.

### **Review Payroll Records for Unusual Matters**

Performing a careful review of the payroll register (that is, the schedule showing the calculation of gross pay, deductions, and net pay) and payroll check register can highlight several types of payroll fraud. We recommend that an appropriate person periodically make such a review, being alert for unusual matters that might suggest fraud, such as the following:

- Duplicate names or addresses.
- Names of former employees.
- Math errors (which may indicate diversion of payroll or payroll taxes).
- Unusual pay rates or numbers of hours worked.
- Factors that may indicate ghost employees.